

OCT 17 2005

FEDERAL ELECTION COMMISSION
999 E Street, N.W.
Washington, D.C. 20463

SENSITIVE

FIRST GENERAL COUNSEL'S REPORT

MUR 5637
DATE COMPLAINT FILED: 1/10/05
DATE OF NOTIFICATION: 1/14/05
DATE ACTIVATED: 5/10/05

EXPIRATION OF STATUTE OF
LIMITATIONS: January 2009

COMPLAINANT: Republican Party of Minnesota

RESPONDENTS: 21st Century Democrats and Michael Lux, in his official
capacity as treasurer
21st Century Democrats ("527 entity")
a/k/a Democrats 2000¹
Matthew K. Entenza

RELEVANT STATUTES: 2 U.S.C. § 434
2 U.S.C. § 441a(f)
2 U.S.C. § 441b(a)
11 C.F.R. § 102.5
11 C.F.R. § 104.10
11 C.F.R. § 106.1
11 C.F.R. § 106.6

INTERNAL REPORTS CHECKED: Disclosure reports
Commission indices

FEDERAL AGENCIES CHECKED: Internal Revenue Service disclosure reports

I. INTRODUCTION

This matter involves allegations that 21st Century Democrats, which has both a federal account registered with the Federal Election Commission ("Commission" or "FEC") and a nonfederal account registered with the Internal Revenue Service ("IRS") under section 527 of the

¹ Both the PAC and the 527 entity were notified of the complaint. The 527 entity, however, filed disclosure reports with the Internal Revenue Service during 2004 under the name Democrats 2000.

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SECRETARIAT

1 Internal Revenue Code, may have used nonfederal donations from Matthew K. Entenza,
2 Democratic-Farmer-Labor Party ("DFL") leader of the Minnesota House of Representatives, to
3 pay for federal campaign activities during the 2004 election cycle.² One of the donations, made
4 by check, was designated for 21st Century Democrats' Young Voter Project ("Voter Project").
5 The Voter Project was a voter mobilization drive targeting young voters in Minnesota, Nevada,
6 Ohio, and Oregon. See 21st Century Democrats' Response at 1.

7 In response to the complaint, 21st Century Democrats acknowledges conducting the Voter
8 Project in the four states mentioned above and receiving Entenza's donations, but it denies
9 violating the Act. It asserts that it allocated its administrative and generic voter drive activities
10 pursuant to 11 C.F.R. §§ 102.5(a) and 106.6, and that it financed the Voter Project's expenses in
11 accord with those provisions.³

12 Although the complaint focuses on donations from a specific donor, it raises the same
13 issue that is raised in certain fact patterns in MURs currently under investigation: whether
14 organizations with both a registered PAC and an unregistered 527 properly allocated costs for
15 voter mobilization activities that were aimed at influencing the 2004 Presidential election. See,
16 e.g., MURs 5403, 5440, and 5466 (America Coming Together).⁴ 21st Century Democrats' own
17 characterization of the Voter Project shows that it was focused on identifying potential John

² References to 21st Century Democrats in this Report include both the federal and nonfederal accounts, unless otherwise specified. The DFL functions as the state committee of the Democratic Party in Minnesota.

³ Specifically, 21st Century Democrats pointed out that its documents and public records show that Entenza's donations were designated for and were deposited into its nonfederal account, and it asserted that the funds were properly used to pay the nonfederal share of allocable activity.

⁴ According to a news account, 21st Century Democrats, like several other organizations that are respondents in the so-called "527 matter" – including America Coming Together, the League of Conservation Voters, and MoveOn.org – participated in the umbrella organization America Votes. See Mark Huntress, *Dean Visits Vote Mob*, The Columbus Free Press (Ohio), October 23, 2004, available at www.freepress.org (last visited September 27, 2005).

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1 Kerry voters in states widely regarded as keys to the Presidential election, registering them, and
2 getting them to the polls, *see Adam Ebbin, 21st Century Democrats Completes 100,000th Voter*
3 *Contact*, August 30, 2004, *available at* <http://www.21stcenturydems.org/> (press release),
4 although a proportion of their direct candidate support may have been for state and local
5 candidates in the course of campaigns to elect Democratic legislative majorities in some states.
6 *See Patrick Sweeney, Big PAC a player in state races; National Group backing DFLers for state*
7 *House*, Saint Paul Pioneer Press (Minnesota), October 14, 2004, at A1. 21st Century Democrats'
8 federal disclosure reports show \$465,970 in allocated disbursements to payees in the four states
9 in which the Voter Project was active that appear to have been for the Voter Project. In addition,
10 IRS Forms 8872 indicate that its 527 account spent \$152,143 in nonfederal funds on payroll and
11 mileage for "field organizers" in at least one of the key states where the Voter Project was
12 conducted. The federal disbursements were allocated on a 10 percent federal/90 percent
13 nonfederal basis. Based on available facts, and consistent with the Commission's actions
14 regarding MURs 5403, 5440, and 5466, this Office recommends that the Commission investigate
15 whether 21st Century Democrats properly allocated its expenditures and disbursements.
16 Consistent with our practice in those cases, we ~~make~~ no recommendations regarding Entenza at
17 this time.⁵

⁵ The complaint alleges that Entenza's donations resulted in excessive federal contributions based on news reports that 21st Century Democrats' federal committee funded the Voter Project. In response to the complaint, Entenza emphasized that his donations were intended exclusively for the "nonfederal" Voter Project, not for any federal election activity or for the support of any specific federal, state, or local candidate. He claims that his donations were all based on information 21st Century Democrats gave him and his resulting belief that the funds would be used exclusively for nonfederal purposes. He did not specify the alleged information he was given.

1 **II. ANALYSIS**

2 **A. Facts**

3 According to publicly available information, 21st Century Democrats was founded in the
4 mid-1980s by U.S. Senator Tom Harkin of Iowa, U.S. Representative Lane Evans of Illinois, and
5 Jim Hightower, a former Texas agriculture commissioner.⁶ See Patrick Sweeney, *supra*. 21st
6 Century Democrats was incorporated as a non-profit corporation in Washington, D.C. on July
7 14, 1988. See <http://dcra.dc.gov> (last visited September 20, 2005). The federal committee
8 registered with the Commission on July 28, 1988 as a nonconnected committee under the name
9 Democrats 2000.⁷ FEC Statement of Organization, July 28, 1988. The IRS website shows that
10 the 527 organization also was originally registered with the IRS under the name Democrats
11 2000; the name there was changed to 21st Century Democrats from January 1, 2001 to December
12 31, 2003 and back to Democrats 2000 from January 1, 2004 to the present.⁸ See
13 <http://forms.irs.gov/politicalOrgsSearch> (last visited September 20, 2005). The organization's
14 IRS Form 8871 (Notice of Section 527 Status) dated August 1, 2000 listed no related entities. *Id.*
15 According to its Form 8871, the 527 organization's purpose is "to elect progressive populist
16 Democrats to office at all levels of government." *Id.*

17 21st Century Democrats' website states that it was "founded to give progressive and
18 populist candidates the support they need to win elections." <http://www.21stcenturydems.org/>
19 (last visited September 20, 2005). According to the website, the organization's "goal is to

⁶ The 527 organization's IRS disclosure reports (Form 8872) state that it was formed on July 1, 1985.

⁷ The committee's name was changed to 21st Century Democrats on March 5, 2001. Statement of Organization, March 7, 2001.

⁸ The IRS website also shows two other organizations with the name "Democrats 2000," but neither of them appears to be related to the respondents in this matter.

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1 transform the Democratic Party by electing candidates who are committed to core progressive
2 values like universal healthcare, public education, fair taxes, corporate accountability, civil
3 rights, and a sustainable environmental policy." *Id.* The organization claims to "build[] the
4 Democratic farm team by electing progressive candidates to all levels of government." *Id.*

5 As previously mentioned, 21st Century Democrats conducted a voter mobilization drive,
6 Voter Project, during the relevant period. An article on its website describes the Voter Project as
7 "the most intense independent campaign ever focused on increasing the Democratic youth
8 vote."⁹ The article also stated that the organization "talked to young people where they live and
9 work, identified potential Democratic voters, managed our data rigorously, and followed up
10 again and again to motivate and educate the young people we talked to." *Id.* at 1. The article
11 described the Voter Project thusly:

12 We created a Get Out The Vote (GOTV) program as intense and effect
13 [sic] as the programs traditionally focused on neighborhoods of reliable
14 Democratic voters. During the campaign, we contacted over 200,000
15 young people; we contacted each voter an average of five times, with three
16 contacts the week of the election providing specific information about how
17 and where to vote; we supplemented in-person and telephone contacts
18 with email messages, text messages, and automated calls; on 31 college
19 campuses, we recruited and supported student leaders who helped us break
20 new ground organizing door-to-door within dorms and residence halls;
21 and we pioneered a new street waving approach called "Vote Mobilizing" -
22 - organizers approached groups of young people wherever we could find
23 them, gathering candidate preferences and personal contact information
24 while asking respondents to sign a pledge to vote.

25 *Id.* at 2.

26 The article touted the success of the Voter Project, noting that "turnout skyrocketed in
27 our targeted precincts," and highlighted success in three states - Ohio, Oregon, and Minnesota.

⁹ *The Silver Lining of 2004: Effective Organizing Turns Out Democratic Young Voters*, available at <http://www.21stcenturydemocrats.org/index.php?submenu=about&are=gendocs&link=youngvoter.cfm&eat>. The article stated that 21st Century Democrats "opened nine field offices in Ohio, Minnesota, Oregon, and Nevada, and hired over thirty full-time organizers and dozens of canvassers and student team leaders." *Id.*

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1 *Id.* In particular, it was noted that in Ohio "Democratic turnout rose in our targeted precincts by
2 an average of 97% over the 2000 election" and that John Kerry won the precincts on the campus
3 of Ohio State University by 187% more votes than Al Gore did in the 2000 Presidential
4 elections. *Id.* The article further stated that in Minnesota "Democratic turnout in our 21
5 targeted precincts increased 80.7%, while Republican turnout increased by only 17%," and that
6 "Kerry won all five precincts by 2% to 14%" in St. Paul, where the organization "targeted five
7 'swing precincts' that split evenly between Bush and Gore in 2000." *Id.* Finally, the article
8 noted that "the youth vote has been called the 'silver lining' for Democrats this year. John
9 Kerry won voters under 30 years old by nine points, 54% to 45%, with greater margins in key
10 swing states. It's the only demographic group Democrats won." *Id.*

11 Although we are not in possession of any printed materials, scripted messages, written
12 instructions, or other kinds of communications relating to the Voter Project, a press release from
13 21st Century Democrats' website indicates that organizers and volunteers focused on John
14 Kerry. In the press release, Kelly Young, Executive Director of 21st Century Democrats,
15 reportedly stated that "over 50% of the young people we have spoken with are strong Kerry
16 supporters, and when combined with 'lean Kerry' young voters, two thirds of the young people
17 we have already spoken with are inclined to vote for progressive candidates." Adam Ebbin,
18 *21st Century Democrats Completes 100,000th Voter Contact*, August 30, 2004, available at
19 <http://www.21stcenturydems.org/>. The press release further specified that 21st Century
20 Democrats had targeted voters and voting precincts and that of the first 99,133 in-person
21 contacts, 51,368 (51%) told organizers they were strong Kerry supporters, 17,301 (17%) were

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1 leaning towards Kerry and 15,251 (15%) were undecided.¹⁰ *Id.* This indicates that 21st Century
2 Democrats engaged in a large voter identification effort, and it may well have later advocated
3 Kerry's election to the individuals identified.

4 At the same time, other statements by Young and other leaders of 21st Century
5 Democrats leave little doubt that the organization engaged in efforts to elect John Kerry and
6 defeat George W. Bush. In a press release on 21st Century Democrats' website, Young
7 reportedly made the following statement: "Young voters will make the decisive difference in
8 this year's election, from winning back the White House to taking back control of state
9 legislatures. I am impressed by the dedication of hundreds of young volunteers - and the
10 commitment of young voters - to electing John Kerry and the Democratic ticket." Adam
11 Ebbin, *New Campaign Offices open in Minnesota, Ohio and Oregon*, August 17, 2004,
12 available at <http://www.21stcenturydems.org/> (emphasis added). Another press release reported
13 that in December 2003 another 21st Century Democrats' official, Jeannie Berg, newly-hired
14 Oregon state director, planned to "recruit[] thousands of activists to knock on doors, make
15 phone calls and talk to voters about defeating Bush in 2004." See Laila Hirschfeld, *21st*
16 *Century Democrats Announce Hire of Oregon State Director*, December 12, 2003, available at
17 <http://www.21stcenturydems.org/> (emphasis added).

18 Schedules H4 filed by 21st Century Democrats covering August through November 2004
19 did not disclose any disbursements for "voter drive" costs. However, many of the
20 organization's reported administrative expenses may have been incurred in connection with the

¹⁰ In particular, the press release also quoted Young as stating: "We've built an operation to identify young voters, we will continue to educate them, and we will make sure they vote in November." It further reported that since mid-June, 21st Century Democrats had "been identifying young voters both at community venues and in targeted precincts," and that "[c]andidates' preferences and personal contact information [] being collected [would] be used to get out the vote with this often hard to reach demographic." *Id.*

1 Voter Project. In the three months before the November 2004 general election, the federal
2 committee disbursed a reported \$465,970 in allocated funds to payees in the four states in which
3 the Voter Project was active. These payments were primarily for such things as payroll,
4 travel/mileage, office rent and office supplies. All these payments were allocated on a 10
5 percent federal/90 percent nonfederal basis. In addition, over the same time period the 527
6 account directly spent \$152,143 in nonfederal funds on payroll and mileage for payees located
7 in Minnesota (but not the other states).

8 At the same time, at least one media account indicates that 21st Century Democrats also
9 may have engaged in more than an insignificant amount of direct candidate support of
10 nonfederal candidates in at least one state, Minnesota. The article stated that 21st Century
11 Democrats was playing a "significant behind-the-scenes role" in "trying to help the Democratic-
12 Farmer-Labor Party win control of the state House," which it quoted the group's chairman of
13 the board -- a former mayor of St Paul -- as characterizing as the organization's "primary goal"
14 in Minnesota. Patrick Sweeney, *supra*. Among the activities the committee reportedly
15 undertook in Minnesota was "paying the salaries of about 20 campaign workers helping DFL
16 candidates," *id.*, which may or may not have had something to do with the reported nonfederal

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1 disbursements to payees in Minnesota.¹¹ Nonetheless, as the chairman also acknowledged in the
2 article, "a high DFL voter turnout and DFL vote is going to affect . . . the congressional and the
3 Kerry campaigns." *Id.*

4 B. Discussion

5 21st Century Democrats had to comply with the then-applicable allocation requirements
6 set forth in 11 C.F.R. part 106. To the extent that 21st Century engaged in "generic" voter
7 mobilization activities that urged the general public to register, vote, or support candidates of a
8 particular party or associated with a particular issue, without mentioning a specific candidate,
9 those costs had to be allocated by using the then-applicable "funds expended" method, which is
10 the ratio of federal expenditures for direct candidate support to the total federal and nonfederal
11 disbursements for direct candidate support made by the committee during the two-year federal
12 election cycle. See 11 C.F.R. §§ 106.6(b)(2)(iii) and 106.6(c) (2004). For purposes of

¹¹ 21st Century Democrats apparently has an affiliated state committee registered with the Minnesota Campaign Finance and Public Disclosure Board ("CFDB"). The two organizations were the subject of two separate proceedings before the CFDB in 2004, one of which apparently clarified the reference in the Sweeney article to "paying the salaries of about 20 campaign workers." The complainant in this matter filed a contemporaneous complaint with the CFDB alleging numerous violations of state campaign finance law by the respondents in this matter and by 21st Century Democrats' Minnesota affiliate. The CFDB found no probable cause to believe that state law was violated, and dismissed the allegations. See www.cfboard.state.mn.us (last visited September 29, 2005). However, as part of its findings of fact, the State Board found that "there is evidence that staff services . . . were provided to the Minnesota DFL State Central Committee by 21st Century Democrats (Minnesota)" and that portions of these same services were in turn "provided to . . . legislative principal campaign committees by the Minnesota DFL State Central Committee." *Id.* If these staff also worked under the Minnesota DFL Party's control on any Federal or allowable activities, questions might arise as to whether 21st Century Democrats made non-Federal contributions to the DFL Party for Federal activity. However, in the absence of further information, we make no recommendations on this issue at this time.

In the other proceeding, which was apparently internally generated, the CFDB found probable cause to believe that the state affiliate accepted contributions in excess of \$100 from 21st Century Democrats on 25 separate occasions dating back to 2001, which violated Minnesota law because 21st Century Democrats is not registered with the CFDB and is thus prohibited by state law from contributing more than \$100 to any entity that is so registered. Counsel for 21st Century Democrats told the CFDB that "21st Century Democrats is a federal PAC that is active on a national basis," and thus "its procedures were not designed specifically to conform to Minnesota procedures." Read in context, this does not appear to be an admission that would affect the analysis in this matter. 21st Century Democrats paid a \$25,000 civil penalty to the CFDB, and its state affiliate paid a \$292,950 civil penalty. See <http://www.cfboard.state.mn.us/bdinfo/investigation/121704-21centnat.pdf> (last visited September 30, 2005).

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1 determining the calculation of the appropriate ratio, Advisory Opinion 2003-37 ("ABC AO")
2 made clear that political committees with nonfederal accounts had to treat costs of
3 communications that promoted, supported, attacked or opposed ("PASO") a clearly identified
4 federal candidate as expenditures.¹² Because it appears that 21st Century Democrats may have
5 treated such expenses as nonfederal disbursements, there is reason to believe it improperly
6 calculated its 90/10 nonfederal to federal allocation ratio.

7 Although a more than incidental proportion of 21st Century Democrats' expenditures for
8 direct candidate support may well have been for state and local candidates, the group's own
9 description of the Voter Project in press releases and other publicity materials -- which
10 emphasizes the election of Kerry and defeat of Bush -- make it appear likely that the 90%
11 nonfederal allocation ratio was too high. 21st Century Democrats' references to candidates
12 Kerry and Bush would not qualify as "generic" voter drives. The costs of voter mobilization
13 messages that promoted or supported Kerry's election, or that attacked or opposed Bush, and in
14 which no nonfederal candidate is clearly identified, should have been paid for with all federal
15 dollars. See 11 C.F.R. § 106.1; see also ABC AO (applying section 106.1 to this kind of voter
16 mobilization activity). References to Bush or Kerry and the entire Democratic Party ticket would
17 require that part of the message be attributed to the clearly identified candidate, with the
18 remaining "generic" part of the message allocable between federal and nonfederal accounts.

¹² The ABC AO interpreted the regulations that were in place at the time of the activity at issue in this matter. Subsequently, in January 2005, the Commission adopted more stringent allocation regulations and, in so doing, superseded the ABC AO. See Explanation and Justification for Regulations on Political Committee Status, Definition of Contribution, and Allocation for Separate Segregated Funds and Nonconnected Committees; Final Rules, 69 Fed Reg. 68,056, 68,063 (November 23, 2004). We are, of course, applying the regulations that were in effect at the time the activity in this matter occurred, rather than the subsequent, more stringent allocation requirements of the January 2005 regulations.

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1 In January 2003, at the beginning of the 2003-04 election cycle, 21st Century Democrats
2 estimated its "funds expended" ratio for the election cycle to be 75 percent nonfederal to 25
3 percent federal. Beginning in June 2004, it adjusted its ratio to 90 percent nonfederal to 10
4 percent federal. Given the Voter Project's apparent focus on the Presidential race, there is reason
5 to believe that 21st Century Democrats and Michael Lux, in his official capacity as treasurer,
6 understated the federal share of any allocable voter mobilization expenses, or used nonfederal
7 funds for communications that should have been paid for under section 106.1 with all federal
8 dollars. Accordingly, this Office recommends that the Commission find reason to believe that
9 21st Century Democrats and Michael Lux, in his official capacity as treasurer, and 21st Century
10 Democrats ("527 entity") a/k/a Democrats 2000, violated 2 U.S.C. §§ 434, 441a(f), and 441b(a);
11 and 11 C.F.R. §§ 102.5, 104.10, and 106.6 by failing to properly allocate and report shared
12 administrative and voter mobilization activities, and by using prohibited funds to pay for the
13 federal share of those expenses, which may have resulted in prohibited and excessive
14 contributions.¹³

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¹³ The IRS disclosure reports show that the nonfederal account accepted union and corporate contributions. In making our recommendations based on an allocation theory, this Office does not foreclose additional recommendations that the 527 organization should itself be registered with the Commission as a political committee, if an investigation uncovers such evidence.

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IV. RECOMMENDATIONS

1. Find reason to believe that 21st Century Democrats and Michael Lux, in his official capacity as treasurer, and 21st Century Democrats ("527 entity") a/k/a Democrats 2000 violated 2 U.S.C. §§ 434, 441a(f), and 441b(a); and 11 C.F.R. §§ 102.5, 104.10, and 106.6, by failing to properly allocate and report shared administrative and voter mobilization activities, and by using prohibited funds to pay for the federal share of those expenses, which may have resulted in prohibited and excessive contributions.
2. Take no action at this time against Matthew K. Entenza.
3. Approve the attached factual and legal analysis.
4. Authorize the use of compulsory process with respect to 21st Century Democrats and Michael Lux, in his official capacity as treasurer, 21st Century Democrats ("527 entity") a/k/a Democrats 2000, and other witnesses, including the issuance of appropriate written questions, document subpoenas, and deposition subpoenas, as necessary.
5. Approve the appropriate letters.

Date

10/17/05


Lawrence H. Norton
General Counsel


Lawrence L. Calvert, Jr.
Deputy Associate General Counsel
for Enforcement

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